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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

COMMISSIONERS**DOCKETED**

DEC -5 2006

JEFF HATCH-MILLER, Chairman
WILLIAM A. MUNDELL
MIKE GLEASON
KRISTIN K. MAYES
BARRY WONG

DOCKETED BY

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IN THE MATTER OF THE APPLICATION OF
DIECA COMMUNICATIONS, INC. D/B/A
COVAD COMMUNICATIONS COMPANY FOR
EXPEDITED APPROVAL TO ENCUMBER
ASSETS IN CONNECTION WITH NEW
FINANCING.

DOCKET NO. T-03632A-06-0215

DECISION NO. 69170**ORDER**

Open Meeting
November 21 and 22, 2006
Phoenix, Arizona

BY THE COMMISSION:

Having considered the entire record herein and being fully advised in the premises, the Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

FINDINGS OF FACT

1. On April 3, 2006, DIECA Communications, Inc., d/b/a Covad Communications Company ("Covad" or "Applicant") filed an application with the Arizona Corporation Commission ("Commission") for authorization to encumber its assets in the State of Arizona in connection with providing its guarantee, or to otherwise provide security in connection with financings of up to \$200 million for its parent, Covad Communications Group, Inc. ("Parent"), pursuant to A.R.S. § 40-285. The stated purpose of the proposed financing is to repay other loans, or for general corporate purposes, capital expenses and working capital, as well as for acquisition of other telecommunication companies and/or telecommunication assets. Covad requests authority for its Parent to pledge a security interest in certain of Covad's assets, including its receivables, tangible personal property, equipment, and intellectual property as collateral security for the debt. The application also states that Covad may participate as a co-borrower.

1 2. On September 27, 2006, Applicant filed a Notice of Filing Affidavit of Publication.

2 3. On October 20, 2006, the Commission's Utilities Division ("Staff") filed a Staff
3 Report recommending conditional approval of the application to pledge assets as a guarantee for new
4 Parent debt, and recommending denial of the request to incur debt.

5 4. Covad, a Virginia Corporation, is a wholly-owned subsidiary of Covad Group.
6 Covad provides fiber optic based competitive data video and internet services to customers in 31
7 states and the District of Columbia. Covad provides integrated voice and data communications, and
8 offers DSL, VOIP, web hosting, managed security, IP and dial-up, and bundled voice and data
9 services nationwide, directly through its network and through internet service providers, value-added
10 resellers, telecommunications carriers, and affinity groups to small and medium sized business and
11 home users.

12 5. Pursuant to Decision No. 61942 (September 19, 1999), Covad was granted authority to
13 provide resold and facilities based local exchange and interexchange telecommunications services
14 throughout Arizona.

15 6. Covad stated in its application that all its physical assets located in Arizona are used
16 only to provide interstate service, that it does not currently provide intrastate services in Arizona.

17 7. Covad has requested authorization to serve as co-borrower for financing up to \$200
18 million and to encumber its assets by providing a guarantee or other security in connection with the
19 financing by itself or the Parent. The proposed financings include a \$50 million revolving line of
20 credit from a commercial bank, as well as a \$50 million investment from Earthlink in return for \$10
21 million of common stock in the Parent and a \$40 million senior secured convertible note. Covad
22 stated that the interest rate will not be determined until each financing is finalized, and will likely be
23 the market rate for similar financing.

24 8. Staff evaluated financial statements provided by Covad under protective agreement,
25 concluded that it is inappropriate for Covad to acquire any new debt, and recommended denial of
26 Covad's request for authorization to participate in any new debt as borrower or co-borrower.

27 9. Staff reviewed the proposed transaction and concluded that Covad and its Parent
28 would benefit from the proposed pledge of assets and guarantee, as it will facilitate the funding of

1 operational activities and is unlikely to have significant detrimental effect on Covad's Arizona
2 customers.

3 10. Based on its review of the proposed transaction, Staff determined that encumbrance of
4 Covad's assets would not impair the financial status of Covad, would not impair its ability to attract
5 capital, and would not impair Covad's ability to provide safe, reasonable and adequate service. Staff
6 stated that alternative service providers are available, and Covad's customers would not experience
7 significant harm in the event that its Parent has financial difficulties.

8 11. Staff recommended approval of Covad's request for authority to pledge assets as a
9 guarantee or to provide other forms of security for the proposed financing of up to \$200 million by its
10 Parent, subject to the condition that all Arizona customer deposits and prepayments be excluded from
11 encumbrance, or in the alternative, that they are secured by a bond which is not included in the
12 pledged collateral.

13 12. Staff recommended authorizing Covad to engage in any transactions and to execute
14 any documents necessary to effectuate the authorizations granted.

15 13. Staff further recommended that Covad be required to provide one copy of all notes,
16 executed security documents, and all other documents memorializing the transactions, to the
17 Compliance Section of the Utilities Division within 60 days of any loan closing.

18 14. Staff stated that Covad has no outstanding compliance issues with the Commission.

19 15. Staff's recommendations are reasonable and should be adopted except that, if Covad
20 does not exclude all Arizona customers deposits and prepayments from encumbrance, we will require
21 Covad to secure those deposits and prepayments either by a bond which is not included in the
22 pledged collateral, as recommended by Staff, or with an irrevocable sight draft Letter of Credit which
23 is not included in the pledged collateral and that is in a form acceptable to Staff.

24 **CONCLUSIONS OF LAW**

25 1. Applicant is a public service corporation within the meaning of Article XV of the
26 Arizona Constitution and A.R.S. §§ 40-281 and 40-282.

27 2. The Commission has jurisdiction over Applicant and the subject matter of the
28 application.

1 3. Notice of the application was given in accordance with the law.

2 4. The pledge of assets as a guarantee, exclusive of customer deposits and prepayments,
3 in support of the Parent's financing up to \$200 million approved herein is for lawful purposes within
4 Covad's corporate powers, is compatible with the public interest, is consistent with sound financial
5 practices, and with the proper performance by Covad of service as a public service corporation, and
6 will not impair Covad's ability to perform that service.

7 5. The encumbrance approved herein is for the purposes stated in the application and is
8 reasonably necessary for those purposes.

9 **ORDER**

10 IT IS THEREFORE ORDERED that the application by DIECA Communications, Inc., d/b/a
11 Covad Communications Company for authorization to encumber assets in connection with new
12 financing for its parent, Covad Communications Group, Inc., as provided for herein, shall be, and
13 hereby is, granted, subject to the condition that all Arizona customer deposits and prepayments be
14 excluded from encumbrance, or in the alternative, that they are secured either by a bond which is not
15 included in the pledged collateral or with an irrevocable sight draft Letter of Credit which is not
16 included in the pledged collateral and that is in a form acceptable to Staff.

17 IT IS FURTHER ORDERED that DIECA Communications, Inc., d/b/a Covad
18 Communications Company's application for authorization to participate, in whole or in part, in the
19 \$200 million debt as borrower or co-borrower shall be, and hereby is, denied.

20 IT IS FURTHER ORDERED that DIECA Communications, Inc., d/b/a Covad
21 Communications Company is hereby authorized to engage in any transactions and to execute any
22 documents necessary to effectuate the financings for which the encumbrance authorization is granted
23 herein.

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1 IT IS FURTHER ORDERED that DIECA Communications, Inc., d/b/a Covad Communications
 2 Company shall provide one copy of all notes, executed security documents and all other documents
 3 memorializing the transactions necessary to effectuate the financings for which the encumbrance
 4 authorization is granted herein to the Compliance Section of the Utilities Division within 60 days of
 5 any loan closing.

6 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

7 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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 9 
 10 CHAIRMAN


 COMMISSIONER

11 
 12 COMMISSIONER


 COMMISSIONER


 COMMISSIONER

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 14 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
 15 Director of the Arizona Corporation Commission, have
 16 hereunto set my hand and caused the official seal of the
 Commission to be affixed at the Capitol, in the City of Phoenix,
 this 5th day of Dec., 2006.

17 
 18 BRIAN C. McNEIL
 19 EXECUTIVE DIRECTOR

20 DISSENT _____

21 DISSENT _____

SERVICE LIST FOR:

DIECA COMMUNICATIONS, INC. D/B/A COVAD
COMMUNICATIONS COMPANY

DOCKET NO.:

T-03632A-06-0215

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